Volume 117
Issue 2 *Dickinson Law Review - Volume 117, 2012-2013*

10-1-2012

Abolishing the Shelter of Ambiguity: A New Framework for Treasury Regulation Deference Clarifying Chevron and Brand X

Sebastian Watt

Abolishing the Shelter of Ambiguity: A New Framework for Treasury Regulation Deference Clarifying *Chevron* and *Brand X*

Sebastian Watt*

Table of Contents

I. INTRODUCTION

Complying with the complex mandates of the Internal Revenue Code (I.R.C.) can be an exhilarating exercise in creative statutory

* J.D. Candidate, The Dickinson School of Law of the Pennsylvania State University, 2013; B.A., University of Mary Washington, 2009. I would like to thank my family, Michael, Georgiana, and Emily, for pushing me to work harder—from elementary school vocabulary flash-cards to law school exams—and for sending me to Wakefield School, The Plains. I need to thank Jessica Case for being there to put up with the law school time-crunch.

interpretation for those who are willing to risk possible penalties.[1] The convolution of the code provides opportunities to take advantage of its provisions, evade taxes, and create complex shelter mechanisms.[2] Tax evasion went uncontrolled in the 1990s, and the tax shelter industry boomed.[3] However, the rise of abusive mechanisms prompted response from both Congress, and the Internal Revenue Service and the U.S. Department of the Treasury ("Treasury").[4]

The Treasury's primary weapon against tax evaders is its congressionally delegated power to interpret the I.R.C. through Treasury Regulations ("TRs").[5] Although the standard of deference due to TRs by the courts has been the subject of academic debate for decades, the U.S. Supreme Court recently determined that courts are to evaluate TRs with the same standard of deference applied to most administrative regulations.[6]

In *Mayo Foundation for Medical Education and Research v. United States*,[7] the Supreme Court held that TRs are entitled to administrative deference as set forth in *Chevron, U.S.A., Inc. v. Natural Resource Defense Counsel*[8] ("*Chevron* deference"), rather than the less deferential standard advocated by some tax practitioners.[9] *Chevron* deference allows a court to defer to an administrative regulation when Congress has not "spoken directly to the precise question at issue" and the regulation is based on a "permissible construction of the statute."[10] By aligning

1. *See* Hale E. Sheppard, *Only Time Will Tell: The Growing Importance of the Statute of Limitations in an Era of Sophisticated International Tax Structuring*, 30 BROOK. J. INT'L L. 453, 453 (2005).

2. *See* Derek B. Wagner, *Who's the (Son of) Boss?: The Struggle Between the Federal Circuit and Treasury to Define "Omits from Gross Income" in Son of Boss Tax Shelters and Other Overstatement-of-Basis Tax Cases*, 21 FED. CIR. B.J. 45, 45 n.1 (2011).

3. *See* Matthew Roche, *Son of Boss and the Troubling Legacy of Colony, Inc. v. Commissioner*, 58 CATH. U. L. REV. 263, 263 (2008).

4. *See id.*

5. *See* I.R.C. § 7805(a) (2006); Roche, *supra* note 3, at 263 (explaining that Congress enabled the Treasury to promulgate regulations to clarify sections of the I.R.C. as necessary for enforcement).

6. *See* Kristin E. Hickman, *The Need for Mead: Rejecting Tax Exceptionalism in Judicial Deference*, 90 MINN. L. REV. 1537, 1560-63 (2006) (discussing the debate in scholarship over the level of deference that the courts should give TRs).

7. Mayo Found. for Med. Educ. & Research v. United States, 131 S. Ct. 704 (2011).

8. Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837 (1984).

9. *See* Richard Lipton & Russell Young, *Courts Split on Validity of Section 6501(e)(1)(A) Regulations After Mayo Foundation*, 115 J. TAX'N 21, 28 (2011) (explaining that *Mayo Foundation* implicitly overruled *Nat'l Muffler Dealers Ass'n v. United States*, 440 U.S. 472 (1979), making *Chevron* the judicial standard for TR deference).

10. *Chevron*, 467 U.S. at 842-43.

judicial deference standards of TRs to the test established in *Chevron*, the Supreme Court indicated that courts are to grant TRs a higher degree of deference than under the pre-*Mayo Foundation* regime.[11]

In the wake of *Mayo Foundation*, several circuits of the U.S. Courts of Appeals are divided over whether deference was due to new TRs interpreting I.R.C. § 6501(e)(1)(A) ("Section 6501").[12] The circuit split demonstrated that *Mayo Foundation* has brought tax deference within the realm of the already problematic *Chevron* jurisprudence.[13] The Supreme Court granted certiorari to resolve the split over Section 6501 and had its first opportunity to clearly examine long-standing *Chevron* problems through a tax lens.[14]

The circuit courts divided over the meaning of Section 6501, a statute of limitations ("SOL") provision that extends the time under which the Treasury can recover tax deficiencies from three to six years when a "taxpayer *omits from gross income* an amount properly includible [on their tax return]. . . ."[15] The circuit courts disagreed whether an overstatement of basis by the taxpayer is included in the statutory meaning of "omits from gross income."[16] Gross income from a sale or exchange is typically the difference between the taxpayer's basis in an item, usually the amount paid, and the amount for which it was sold.[17]

---

11. *See generally* Carpenter Family Invs., LLC v. Comm'r, 136 T.C. 373, 389 (2011) (discussing the effect of *Mayo Foundation* on TR jurisprudence).

12. *See* Burks v. United States, 633 F.3d 347 (5th Cir. 2011); Home Concrete & Supply, LLC v. United States, 634 F.3d 249 (4th Cir. 2011), *aff'd*, 132 S. Ct 1836 (2011); Grapevine Imports, Ltd. v. United States, 636 F.3d 1368 (Fed. Cir. 2011); Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929 (10th Cir. 2011); Intermountain Ins. Serv. of Vail v. Comm'r, 650 F.3d 691 (D.C. Cir. 2011).

13. *See* Richard Lipton & Russell Young, *Treasury Regulations, and the 'Death' of National Muffler*, 114 J. TAX'N 206, 214 (2011) ("[T]he ghost of *National Muffler* still may benevolently haunt post-*Mayo Foundation* cases.").

14. *See* Carpenter Family Invs., LLC v. Comm'r, 136 T.C. 373, 389-90 (2011); Home Concrete & Supply, LLC v. United States, 634 F.3d 249 (4th Cir. Feb. 2011), *aff'd*, 132 S. Ct 1836 (2011).

15. I.R.C. § 6501 (2006) (emphasis added). The statute was amended in 2010 by the Hiring Incentives to Restore Employment Act of 2010, Pub. L. No. 111-147, § 513(a)(1), 124 Stat. 1. *See Salman Ranch IV*, 647 F.3d at 933 n.8. I.R.C. § 6501(e)(1)(A)(i-ii), the gross receipts and adequate disclosure provisions, was moved to I.R.C. § 6501(e)(1)(B)(i-ii) to make room for clarification of an unrelated matter. *See id.* In accordance with the courts discussed in this Comment, references to Section 6501 refer to the 2006 version of the I.R.C. *See id.* (noting that courts and parties consistently refer to the pre-amended version of the Section).

16. *See* Treas. Reg. §§ 301.6501(e)-1, 301.6229(c)(2)-1 (as amended by T.D. 9511, 75 Fed. Reg. 78897-01 (Dec. 17, 2010)).

17. *See* I.R.C. § 61(a) (2006); I.R.C. § 1001(a) (2006) ("Computation of gain or loss.—The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 1011 for determining gain, and the loss shall be the excess of the adjusted basis provided in such section for determining loss over the amount realized.").

Therefore, a taxpayer could reduce his tax liability by either understating his income or overstating his basis because both would reduce the total amount of tax liability owed.[18]

Although the Supreme Court had interpreted Section 6501 before, the circuit courts were divided over whether they were bound by the precedent, or could distinguish it.[19] In 1958, the Supreme Court, in *Colony v. Commissioner*,[20] held that an overstatement of basis was not included within the definition of "omits from gross income."[21] According to the Court, only an understatement of income, not an overstatement of basis, would extend the SOL from three to six years.[22] A month before the Supreme Court's 2011 decision in *Mayo Foundation*, the Treasury attempted to distinguish *Colony* by issuing TRs that re-interpreted "omits from gross income" under Section 6501. The Treasury distinguished *Colony*, arguing that the case spoke only to taxpayers who were a "trade or business" engaged in "the sale of goods or services. . . ."[23] Thus, outside the trade or business context, the statute was ambiguous, allowing the Treasury to issue interpretive TRs.[24]

Since then, two circuit courts have held the TRs to be invalid and have found that *Colony* controls without exception, applying a three-year SOL when a taxpayer reduces his tax liability by overstating basis.[25] Conversely, three other circuit courts have held that the TRs controls, thus allowing the Treasury six years to prosecute taxpayer deficiencies under the section.[26] The Supreme Court resolved the split in *Home*

18. *See* I.R.C. § 1001(a) (2006).

19. *See generally* Home Concrete & Supply, LLC v. United States, 634 F.3d 249, 254-55 (4th Cir. 2011) (discussing the circuit split), *aff'd*, 132 S. Ct 1836 (2011).

20. Colony, Inc. v. Comm'r, 357 U.S. 28 (1958).

21. *See id.* at 36-37.

22. *See id.*

23. I.R.C. § 6501(e)(1)(A)(i) (2006); *see* Treas. Reg. §§ 301.6501(e)-1, 301.6229(c)(2)-1 (as amended T.D. 9511, 75 Fed. Reg. 78897-01 (Dec. 17, 2010)). The regulations interpreted both I.R.C. § 6501(e) and I.R.C. § 6229(c). *See id.* Although the provisions differ slightly, courts focus on the interpretation of Section 6501 because the statutes are interdependent. *See, e.g.*, Salman Ranch Ltd. v. United States (Salman Ranch I), 79 Fed. Cl. 189, 193 (2007). Although Section 6501 applies to a "trade or business" engaged in "the sale of goods or services," this Comment will omit "the sale of goods or services" language of the reference to comport with courts' treatment of the limitation in their discussions. *See, e.g.*, *Home Concrete*, 634 F.3d at 254-55 (referring to Section 6501 as applying to a "trade or business" and omitting "the sale of goods or services").

24. *See* Treas. Reg. §§ 301.6501(e)-1, 301.6229(c)(2)-1 (as amended T.D. 9511, 75 Fed. Reg. 78897-01 (Dec. 17, 2010)).

25. *See* Burks v. United States, 633 F.3d 347 (5th Cir. 2011); Home Concrete & Supply, LLC v. United States, 634 F.3d 249 (4th Cir. 2011), *aff'd*, 132 S. Ct 1836 (2011).

26. *See* Grapevine Imports, Ltd. v. United States, 636 F.3d 1368 (Fed. Cir. 2011); Intermountain Ins. Serv. of Vail v. Comm'r, 650 F.3d 691 (D.C. Cir. 2011); Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929 (10th Cir. 2011); *see also*

Concrete & Supply v. United States[27] by deciding not to extend the SOL in any context, holding that *Colony* resolved the ambiguity and that overstating basis does not result in "omit[ing] from gross income."[28] However, the majority rested its decision on *stare decisis* rather than taking the opportunity to resolve a long-standing question in administrative law: to what extent does the ambiguity determination of a pre-*Chevron* decision bind a court determining statutory ambiguity post-*Chevron*?

In *National Cable & Telecommunications Association v. Brand X Internet Services*,[29] the Supreme Court held that "[a] court's prior judicial construction of a statute trumps an agency construction otherwise entitled to *Chevron* deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion."[30] However, lower courts have applied *Brand X* inconsistently due to their inability to determine when a prior court decision made a determination of a statute's ambiguity.[31]

This Comment will address the failure of *Brand X* to produce consistent results in the context of the conflict between *Colony* and the Section 6501 TRs. Specifically, this Comment will argue that the recent circuit split over Section 6501 demonstrates the inability of the courts to apply *Brand X* with consistency.[32] Part II of this Comment will discuss the impact of *Chevron* and *Mayo Foundation* to TR deference, analyze the Supreme Court's interpretation of Section 6501 in *Colony*, and provide a case, *Salmon Ranch v. Commissioner*,[33] exemplifying the tax-evading transactions at issue in Section 6501 cases.

Beard v. Comm'r, 633 F.3d 616 (7th Cir. 2011) (extending the SOL to six years without reaching the validity of the Section 6501 TRs).

27. United States v. Home Concrete & Supply, LLC, 132 S. Ct. 1836 (2012).

28. *See Home Concrete*, 132 S. Ct 1836, 1839 (2011).

29. Nat'l Cable & Telecomms. Ass'n. v. Brand X Internet Servs., 545 U.S. 967 (2005).

30. *Id.* at 982.

31. *See, e.g.*, Robin K. Craig, *Agencies Interpreting Courts Interpreting Statutes: The Deference Conundrum of a Divided Supreme Court*, 61 EMORY L.J. 1, 18-24 (2011) (comparing courts that deferred to agency regulation over precedent to those who did not).

32. *See Administrative Law*—Chevron *Deference—Federal Tax Court Holds Pre-*Chevron *Judicial Construction of Statute Precludes Subsequent Agency Interpretation if Prior Construction Was Premised on Legislative History*, 124 HARV. L. REV. 1066, 1066-67 (2011) (using the Section 6501 circuit split to argue for a new *Brand X* framework).

33. Salman Ranch, Ltd. v. United States (Salman Ranch I), 79 Fed. Cl. 189 (2007); Salman Ranch, Ltd. v. United States (Salman Ranch II), 573 F.3d 1362 (Fed. Cir. 2009); Salman Ranch, Ltd. v. Comm'r (Salman Ranch III), No. 13677–08 (T.C. Aug. 7, 2009); Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929 (10th Cir. 2011).

Part III will argue that *Brand X*, the case in which the Supreme Court attempted to answer the question of when a court is bound by a pre-*Chevron* determination of statutory ambiguity, is an important, yet ambiguous precedent. Indeed, the circuit split over whether a court is bound by *Colony* demonstrates that *Brand X* is ambiguous, at best, and cannot be applied consistently.[34]

Finally, Part III posits that courts will only achieve consistency if a prior determination of statutory ambiguity is consistently construed narrowly. That is, courts can achieve consistency by distinguishing judicial precedent in favor of agency regulation when courts attempt to determine if they are bound by a pre-existing determination of statutory ambiguity. Such a framework would yield consistent results in lower courts and be faithful to *Chevron*'s deferential framework.[35]

II. BACKGROUND

The Section 6501 circuit split demonstrated that *Brand X*, the case that attempted to answer when a court is bound by a prior determination of statutory ambiguity, is an unworkable precedent. To understand how *Brand X* fits into the circuit split, Section A of this Part will detail the level of judicial deference due to TRs generally. Section B will examine *Colony*, where the Supreme Court made its first determination regarding statutory ambiguity in Section 6501. Part C will then discuss *Salman Ranch v. Commissioner*[36] to exemplify the types of transactions that are at issue in Section 6501 cases and why the Treasury promulgated TRs interpreting the section differently than the Supreme Court in *Colony*.

A. Chevron Deference Prevails in Mayo Foundation

Congress, through the I.R.C., delegates legislative authority to the Treasury to promulgate rules in varied forms.[37] However, the precise level of deference has been at issue for years.[38]

---

34. *See infra* Parts III.B-C.

35. *See infra* Part III.E.

36. Salman Ranch, Ltd. v. United States (Salman Ranch I), 79 Fed. Cl. 189 (2007); Salman Ranch, Ltd. v. United States (Salman Ranch II), 573 F.3d 1362 (Fed. Cir. 2009); Salman Ranch, Ltd. v. Comm'r (Salman Ranch III), No. 13677–08 (T.C. Aug. 7, 2009); Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929 (10th Cir. 2011).

37. *See* I.R.C. § 7805(a) (2000); *see generally* Donald L. Korb, *The Four R's Revisited: Regulations, Rulings, Reliance, and Retroactivity in the 21st century: A View from Within Mitchell Rogovin (1931-1996) Chief Counsel, Internal Revenue Service 1965-1966*, 46 DUQ. L. REV. 323, 326 (2008) (discussing the Treasury's varied types of regulations and the authority under which they are promulgated).

38. *See* Andrew Pruitt, *Judicial Deference of Retroactive Interpretative Treasury Regulations*, 79 GEO. WASH. L. REV. 1558, 1575 (2011) (describing judicial deference case law as confusing and unresolved).

In 1979, the Supreme Court examined the proper deference that courts should apply to TRs in *National Muffler Dealers Association v. United States*.[39] The Court held: "In determining whether a particular regulation carries out the congressional mandate in a proper manner, we look to see whether the regulation harmonizes with the plain language of the statute, its origin, and its purpose."[40] The Court articulated factors to determine whether an agency construction of an I.R.C. statute was valid. These factors included the regulation's evolution, its effective longevity, reliance, consistency of Treasury interpretation, and congressional examination of the regulation in legislative changes.[41]

In *Chevron*, a case unrelated to the I.R.C., the Supreme Court determined that agency regulations were generally evaluated under a two-part test.[42] First, a court must ask "whether Congress has directly spoken to the precise question at issue."[43] If the statute "unambiguously expressed [the] intent of Congress," then the agency may not regulate on the specific issue.[44] Second, if the court finds that the statue is "silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute."[45] If the agency regulation is reasonable, the court is required to defer to the regulation.[46]

Until 2011, it was unclear whether TRs warranted the multi-factor *National Muffler* analysis, or the two-step *Chevron* analysis.[47] Courts inconsistently cited both cases when reviewing TRs.[48] However, in *Mayo Foundation*, the Supreme Court explicitly held that the TRs were entitled to *Chevron* deference.[49]

Mayo Foundation concerned the validity of a TR excluding medical residents working 50 to 80 hours per week from a specific student tax exemption.[50] Using the factors set out in *National Muffler*, the District

39. Nat'l Muffler Dealers Ass'n v. United States, 440 U.S. 472 (1979).

40. *Id.* at 477.

41. *Id.*; *see* Hickman, *supra* note 6, at 1559.

42. Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 837 (1984).

43. *Chevron*, 467 U.S. at 842.

44. *Id.*

45. *Id.* at 843.

46. *See id.* at 844 ("A court may not substitute its own construction of a statutory provision for a reasonable interpretation made by the administrator of an agency.").

47. *See* Hickman, *supra* note 6, at 1538 (arguing that neither academics nor the courts had determined the proper standard for TR deference by the time of the article's publication and arguing that they should be evaluated under the *National Muffler* standard).

48. *See* Mayo Found. for Med. Educ. & Research v. United States, 131 S. Ct. 704, 712 (2011).

49. *See id.* at 710.

50. *See id.* at 708-10; Treas. Reg. § 31.3121(b)(10) (2005).

Court concluded that the TR was "inconsistent with the unambiguous text of § 3121 . . ." and granted summary judgment for the taxpayer.[51] The Supreme Court disagreed, holding that the Treasury's interpretation of the statute was entitled to *Chevron* deference.[52] The Court explicitly adopted the two-step *Chevron* analysis as the standard to evaluate TR deference.[53]

Although *Mayo Foundation* announced that *Chevron* deference applies to TRs, Section 6501 cases demonstrated that *Chevron* deference itself is an unsettled framework.[54] Specifically, circuit courts disagreed as to the proper level of deference due to a prior determination of statutory ambiguity in their *Chevron* analysis, an issue that *Brand X* attempted to resolve.[55] The application of *Brand X* by courts in the circuit split centers on the binding effect of the Supreme Court's 1958 case in *Colony*.[56]

B. *The Supreme Court's Determination of Section 6501 Ambiguity:* Colony v. Commissioner

The controversy over Section 6501 began when the circuit courts divided over the 1939 version of the I.R.C.[57] The 1939 I.R.C. extended the SOL that the Commissioner of Internal Revenue ("Commissioner") had to assess income tax deficiencies from three to five years when the taxpayer "[*omitted*] *from gross income* an amount properly includible

51. *See Mayo Found.*, 131 S. Ct. at 710.

52. *See id.* at 713.

53. *See id.* The Court rejected the argument that administrative tax law is exceptional, thus rejecting a less deferential standard of review for TRs. *See id.*; *see also* Hickman, *supra* note 6, at 1600 (arguing against a special rule for TRs outside of the *Chevron* framework). The Court also rejected the argument that TRs authorized by general authority delegation under I.R.C. § 7805(a) to "prescribe all needful rules and regulations for the enforcement" of the I.R.C., like those at issue in *National Muffler*, warranted less deference than when issued under the Treasury's specific authority. I.R.C. § 7805(a); *see Mayo Found.*, 131 S. Ct. at 713-14.

54. *See* Lipton & Young, *supra* note 13, at 206 (recognizing that, after *Mayo Foundation*, courts are to evaluate deference according to the *Chevron*, rather than the *National Muffler*, standard). *Compare* Home Concrete & Supply, LLC v. United States, 634 F.3d 249, 257 (4th Cir. 2011) (applying *Colony* as a *Chevron* step-one holding), *aff'd*, 132 S. Ct 1836 (2011), *with* Grapevine Imports, Ltd. v. United States, 636 F.3d 1368, 1380 (Fed. Cir. 2011) (applying *Colony* as a *Chevron* step-two holding).

55. *See infra* Part III.A; *see also* Lipton & Young, *supra* note 13, at 206 (2011) ("[T]he first two courts of appeals to analyze Regulations under the *Mayo Foundation* standard [*Home Concrete* and *Burks v. United States*, 633 F.3d 347 (5th Cir. 2011)] declined to apply the Regulations in question.").

56. *See Home Concrete*, 634 F.3d at 251.

57. *See* I.R.C. § 275(c) (1939); Colony, Inc. v. Comm'r, 357 U.S. 28, 29 (1958) (examining the divide between the circuit courts).

therein. . . ."[58] In *Colony*, the Commissioner issued deficiencies to Colony, Inc., a real estate developer in Lexington, Kentucky, for the 1946 and 1947 tax years, shortly before the five-year SOL expired.[59] The Commissioner argued that the taxpayer understated the profits of residential land lots by including unallowable development expenses in the calculation of the lots' basis.[60]

The Supreme Court resolved the case by concluding that an overstatement of basis did not extend the statutory SOL from three to five years.[61] The Court found that the statute reasonably lent itself to the taxpayer's interpretation—that overstating basis was a result of mistakenly including unallowable expenses in the calculation of basis—and that the mistake was not an "omission" from the tax return.[62] The Court began its analysis by noting, "[I]t cannot be said that the language is unambiguous."[63] After this admission, examining the legislative history of the statute, and resolving the case for the taxpayer, the Court "observe[d] that the conclusion we reach is in harmony with the *unambiguous* language of section 6501(e)(1)(A) of the Internal Revenue Code of 1954."[64]

The 1954 version of the I.R.C. that the Court referred to as being "in harmony" with its decision in *Colony* included I.R.C. § 6501(e)(1)(A)(i), which is referred to as the gross receipts provision. The gross receipts provision defines "gross income" when the taxpayer is not a "trade or business" engaged in the "sale of goods or services."[65] In subsequent litigation, the Treasury has emphasized *Colony*'s reference to the gross receipts provision to argue that the Court's holding was limited

58. I.R.C. § 275(a) (1939) (emphasis added). The 1939 code extended the SOL from three to five years. *Id.* The current statute extends the SOL from three to six years. I.R.C. § 6501(e)(1)(A) (2006).

59. *See* Colony, Inc. v. Comm'r, 26 T.C. 30, 31 (1956), *aff'd*, 244 F.2d 75 (6th Cir. 1957), *rev'd*, 357 U.S. 28 (1958).

60. *See Colony*, 357 U.S. at 31; I.R.C. § 1001(a) (2006).

61. *See Colony*, 357 U.S. at 38.

62. *See id.* at 37.

63. *Id.* at 32-33.

64. *Id. at* 31-37 (emphasis added). The Court focused on the legislative committee's use of the words "leave out" and "omit." *Id.* at 33-36. The Court noted that the conclusion it reached under the prior version of Section 6501, I.R.C. § 275 (1939), was in harmony with its successor provision, Section 6501. *Id.* at 37. This statement, in combination with the Court's previous statement that the statute was not "unambiguous," and the Court's examination of legislative history, has become integral to later courts' examination of the binding nature of the case. *See, e.g.*, Grapevine Imports, Ltd. v. United States, 636 F.3d 1368, 1378 (Fed. Cir. 2011) (noting the *Colony* Court's inconsistent language).

65. *See* I.R.C. § 6501(e) (2006); *Colony*, 357 U.S. at 37 n.3.

to trades or businesses engaged in the sale of goods or services.[66] Although the Treasury eventually promulgated Section 6501 TRs in 2010 limiting Section 6501, the circuit courts before the TRs focused entirely on the language of the statute and reasoning in *Colony*.[67]

C. *The Circuit Court's Treatment of Section 6501 and Colony Before Section 6501 Treasury Regulations*

Section 6501 became increasingly important in the last decade as the government attempted to recover revenue hidden by taxpayers in Bond Option Sales Strategy ("Son-of-BOSS") tax shelters.[68] The Son-of-BOSS tax shelter was used to hide billions of dollars from the Treasury.[69] A taxpayer uses a series of transactions with contingent liabilities to artificially inflate basis, and thus reduce the taxable gains realized when sold.[70] The Treasury eventually closed the loophole that allowed these transactions and offered participants an opportunity to pay

---

66. *See, e.g.*, Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929, 937 (10th Cir. 2011) ("The first step of *Chevron* requires us to ask whether Congress's intent is clear with respect to whether the phrase 'omits from gross income an amount' in § 6501(e)(1)(A) includes overstatements of basis arising outside of the trade-or-business context."). The Treasury's argument emanates from the language of the statute at issue in *Colony*:

> (A) General rule.—If the taxpayer omits from gross income an amount properly includible therein which is in excess of 25 percent of the amount of gross income stated in the return, the tax may be assessed, or a proceeding in court for the collection of such tax may be begun without assessment, at any time within 6 years after the return was filed. For purposes of this subparagraph—
>
> (i) In the case of a trade or business, the term "gross income" means the total of the amounts received or accrued from the sale of goods or services (if such amounts are required to be shown on the return) prior to diminution by the cost of such sales or services; and
>
> (ii) In determining the amount omitted from gross income, there shall not be taken into account any amount which is omitted from gross income stated in the return if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the Secretary of the nature and amount of such item.

I.R.C. § 6501(e)(1) (2006). I.R.C. § 6501(e)(1)(A)(i) is the gross receipts provision, from which the trade or business exception emanates, whereas I.R.C. § 6501(e)(1)(A)(ii) is the gross receipt provision from which the adequate disclosure exception emanates. *See* Roche, *supra* note 3, at 278-89.

67. *See* Treas. Reg. §§ 301.6501(e)-1, 301.6229(c)(2)-1 (as amended by T.D. 9511, 75 Fed. Reg. 78897-01 (Dec. 17, 2010)); *see* Salman Ranch, Ltd. v. United States (Salman Ranch II), 573 F.3d 1362, 1372-77 (Fed. Cir. 2009). On the other hand, since 2011, the circuit courts have focused on the validity of the TRs. *See, e.g.*, Grapevine Imports, Ltd. v. United States, 636 F.3d 1368 (Fed. Cir. 2011) (upholding the TRs). *But see* Beard v. Comm'r, 633 F.3d 616, 623 (7th Cir. 2011) (concluding that the six-year SOL applied before reaching the question of TR validity).

68. *See generally* Wagner, *supra* note 2, at 46-48.

69. *See id.*

70. *See id.*

their deficiencies with interest and a small penalty.[71] As the IRS attempted to litigate against the taxpayers who did not participate in the settlement, they ran into Section 6501 SOL problems.[72] The three-year SOL inhibited the Treasury's efforts to recoup billions of dollars hidden by these gain-sheltering transactions.[73] Before the promulgation of the Section 6501 TRs, the ability of the Treasury to invoke the six-year SOL hinged entirely on the judicial interpretation of Section 6501 and *Colony*.[74]

Some courts applied *Colony* without exception, declining to extend the SOL whenever the deficiency resulted from an overstatement of basis.[75] Others granted the Treasury relief by limiting *Colony* to the trade or business exception.[76] The *Salman Ranch* cases demonstrated these approaches, how taxpayers took advantage of Section 6501, and the frustration that the IRS faced when litigating deficiencies under the

71. *See id.*

72. *See id.*

73. *See id.* at 51 (concluding that, as of 2011, 35 to 50 Son-of-BOSS transactions and over a billion dollars remained in pending litigation).

74. *See, e.g.*, Salman Ranch Ltd. v. United States (Salman Ranch I), 79 Fed. Cl. 189, 194-96 (2007) (focusing on *Colony* to determine that Section 6501 did extend the SOL to six years).

75. *See* Bakersfield Energy Partners v. Comm'r, 568 F.3d 767, 778 (9th Cir. 2009); Salman Ranch, Ltd. v. United States (Salman Ranch II), 573 F.3d 1362, 1377 (Fed. Cir. 2009).

76. *See* Beard v. Comm'r, 633 F.3d 616, 621 (7th Cir. 2011); Brandon Ridge Partners v. United States, 2007 WL 2209129, at *6-7 (M.D. Fla. July 30, 2009). In applying the gross receipts provision of I.R.C. § 6501(e)(1)(A)(i) (2006), a court limits *Colony* to "omissions of income derived only from the sale of goods or services by trades or businesses." *See* Roche, *supra* note 3, at 296. Some courts also limited *Colony* using the adequate disclosure test, derived from the adequate disclosure provision of I.R.C. § 6501(e)(1)(A)(ii) (2006) (which has not been an issue in the 2011 circuit split), in which a court asks whether or not the taxpayer placed the Commissioner at a "special disadvantage" in determining if something was omitted from the return. *See id.* at 278-79. Congress also provided some relief to the Treasury by amending I.R.C. § 6501(c) (2000) in 2004 to expand the SOL for fraudulent "listed transactions." *See id.* at 291. However, many cases remain subject to Section 6501 and *Colony*. The American Jobs Creation Act of 2004, Pub. L. 108-357, 118 Stat 1418, "tightened the rules relating to tax shelters by replacing the existing tax shelter registration regime with a disclosure regime that is supported by stiff penalties for tax shelter participants." *Id.* (footnote omitted). The American Jobs Creation Act amended I.R.C. § 6501(c) by adding a provision that extended the SOL to one year after disclosure to the Treasury when the taxpayer "fails to disclose a listed transaction." *Id.* However, the narrow focus of I.R.C. § 6501(c)'s anti-fraud SOL has left most cases subject to the I.R.C. § 6501(e) determination that Congress failed to amend. *Id.*

statute.[77] *Salman Ranch* has been litigated four times in two different circuits.[78]

In 1987, owners of Salman Ranch in Mora County, New Mexico, formed Salman Ranch, Ltd., a limited partnership with four principle shareholders.[79] In 1998, three of the four principle shareholders created new, separate limited partnerships.[80] The following year, each of the Salman Ranch partners conducted short-sale[81] transactions of U.S. Treasury Notes and sold them to a third party for a combined $10,982,373.[82] Several days later, each of the individual partnerships transferred the proceeds from the short-sale, and the corresponding short positions, to the Salman Ranch partnership.[83] Following the transfer, Salman Ranch closed the short position by purchasing the Treasury Notes for $10,980,866.[84]

Each of the three Salman Ranch partners contributed their portion of their ownership in the Salman Ranch partnership to newly formed individual limited partnerships.[85] This transaction technically terminated the Salman Ranch partnership, allowing the individual partnerships to elect to increase their basis in the Salman Ranch partnership by including the amount of the proceeds earned in the short-sale.[86] Thus, each partner's new basis in Salman Ranch's final tax return after its technical termination included proceeds from the short-sale without taking into account the corresponding obligation to close the short-sale.[87] Thereafter, the partnership sold part of the ranch, and an option to

77. *See generally* Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929, 931-37 (10th Cir. 2011) (discussing the transactions at issue and the procedural posture of the four cases involving the Salman Ranch partnership).

78. *See id.*

79. *Salman Ranch I*, 79 Fed. Cl. at 191 (2007).

80. *Id.*

81. *See generally* Bernard J. Audet, Jr., *One Case to Rule Them All: The Ninth Circuit in Bakersfield Applies Colony to Deny the IRS an Extended Statute of Limitations in Overstatement of Basis Cases*, 55 VILL. L. REV. 409, 410 n.6 (2010) (explaining a short-sale transaction). In a short-sale transaction, a taxpayer borrows a security from a broker and sells them for cash to a third party. *See id.* This sale creates an obligation, termed a "short position," to replace (or "close") the broker's security. *See id.* The taxpayer profits from the transaction if the market price of the security falls before he must replace it with the broker. *See id.*

82. *Salman Ranch I*, 79 Fed. Cl. at 191.

83. *Id.* at 190.

84. *Id.* The slight difference between the amount that the bonds were sold for and closed for reflected a change in the market price for the bonds. *See id.*

85. *Id.* at 191.

86. *Id.* The partnership was automatically terminated pursuant to I.R.C. § 708(b)(1)(B) (2006), thus allowing the partners to adjust their basis pursuant to I.R.C. §§ 754 and 734(b)(1) (2006). *See Salman Ranch I*, 79 Fed. Cl. at 191.

87. *Id.*

purchase the remainder, for $7,088,588.[88] Salman Ranch filed its tax return for 1999 on April 16, 2000, reporting proceeds from the sale of $7,188,588.00, and a cost basis of $6,850,276—a taxable gain of $338,312.[89]

The IRS issued an administrative deficiency notification—a Final Partnership Administrative Adjustment (FPAA), on April 10, 2006—just before the six-year SOL on Salman Ranch's 1999 return expired.[90] The FPAA notified the taxpayer that it had overstated its basis in its 1999 tax return, resulting in a $4,567,949 deficiency in reported capital gain income of the partnership.[91] The IRS based its conclusion on the failure of the partnership to offset its basis in the short-sale by the corresponding obligation to close the transaction.[92]

In *Salman Ranch, Ltd. v. United States (Salman Ranch I)*,[93] the partnership brought an action in the United States Court of Federal Claims, arguing that the FPAA was untimely because it was issued after the expiration of the three-year SOL under Section 6501.[94] The case turned on whether "omits from gross income" under the Section applied to an overstatement of basis.[95] The Court held for the Commissioner, applying the six-year SOL.[96] The Court applied the trade or business exception by construing gross income as receipts from a trade or business engaged in the sale of goods or services.[97] Thus, the Court reasoned that Salman Ranch was not bound by *Colony* because the partnership was not, like the taxpayer in *Colony*, a trade or business within the meaning of the statute.[98]

---

88. *Id.*

89. *Id.* By increasing their basis in the partnership, the partners were able to reduce the difference between the amount realized from the short-sale and the adjusted basis, thereby reducing the partners' tax liability. *See* I.R.C. § 1001 (2006) ("The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis. . . .").

90. *Salman Ranch I*, 79 Fed. Cl. at 191.

91. *Id.*

92. *Id.*

93. Salman Ranch Ltd. v. United States (Salman Ranch I), 79 Fed. Cl. 189 (2007).

94. *Id.* at 190. The partners paid the deficiency and filed a claim to obtain a refund for the amount paid. *See id.*

95. *See id.* at 193.

96. *See id.* at 204.

97. *See id.* at 200-203; I.R.C. § 6501(e)(1)(A)(i-ii) (2006). It was in relation to this trade or business provision that the Supreme Court in *Colony* "observe[d] that the conclusion [they reached was] in harmony with the unambiguous language of s [sic] 6501(e)(1)(A) of the internal revenue code of 1954." Colony v. Comm'r, 357 U.S. 28, 37 (1958).

98. *See Salman Ranch I*, 79 Fed. Cl. at 200-03. The court also dismissed Salman Ranch's argument that they were entitled to the three-year SOL because they adequately disclosed the nature of the transaction pursuant to I.R.C. § 6501(e)(1)(A)(ii) (2006). *See id.* at 204.

On appeal, in *Salman Ranch, Ltd. v. United States (Salman Ranch II)*,[99] the Federal Circuit reversed, holding that the three-year SOL applied, and the recovery of any deficiency in the 1999 tax return was time-barred.[100] The Court refused to limit *Colony* to taxpayers who were trades or businesses.[101]

In *Salman Ranch v. Commissioner (Salman Ranch III)*,[102] the controversy was litigated in the Tax Court. *Salman Ranch III* concerned Salman Ranch's 2001 and 2002 returns.[103] The case was appealed and heard by the Tenth Circuit in *Salman Ranch v. Commissioner (Salman Ranch IV)*.[104] The tax returns at issue reported the buyer's exercise of the option to purchase the remainder of Salman Ranch's land from the 1999 transaction.[105] Again, the IRS issued a FPAA almost six years after Salman Ranch filed the return.[106] The IRS determined that, after the partners' basis was properly reduced, the partnership's taxable income would increase by $1,331,281 in 2001 and $3,524,010 in 2002.[107] The Tax Court sided with the taxpayer, holding that the three-year SOL applied.[108]

After the Tax Court's decision in *Salman Ranch III*, but before the appeal concluded in the Tenth Circuit's decision in *Salman Ranch IV*, the IRS exercised its general statutory authority and promulgated Section 6501 TRs to bolster their position in the ongoing litigation.[109] The Treasury issued temporary TRs on September 28, 2009,[110] and final TRs

99. Salman Ranch Ltd. v. United States (Salman Ranch II), 573 F.3d 1362 (Fed. Cir. 2009).

100. *See id.* at 1363.

101. *See id.* at 1373-75. The court also refused to apply the adequate disclosure test of I.R.C. § 6501(e)(1)(A)(ii) (2006). *See id.*

102. Salman Ranch, Ltd. v. Comm'r (Salman Ranch III), No. 13677–08 (T.C. Aug. 7, 2009).

103. Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929, 932 (10th Cir. 2011).

104. *Id.* at 929.

105. *Id.* at 932.

106. *Id.* at 933.

107. *Id.*

108. *See id.* at 935 (noting that the Tax Court explicitly followed its prior decision in Bakersfield Energy Partners v. Comm'r, 128 T.C. 207 (2007), *aff'd*, 568 F.3d 767 (9th Cir. 2009)).

109. *See* Treas. Reg. §§ 301.6501(e)-1, 301.6229(c)(2)-1 (as amended T.D. 9511, 75 Fed. Reg. 78897-01) (Dec. 17, 2010)). Some parties have argued that issuing regulations during ongoing litigation should be invalid. *See, e.g.*, *Salman Ranch IV*, 647 F.3d at 940. However, the Supreme Court rejected this argument in *Mayo Foundation*. *See* Mayo Found. for Med. Educ. & Research v. United States, 131 S. Ct. 704, 712-13 (2011).

110. Temp. Treas. Reg. §§ 301.6229(c)(2)-1T(b), 301.6501(e)-1T(b) (as amended by T.D. 9466) (effective Sept. 24, 2009 to Dec. 13, 2010).

on December 14, 2010.[111] The Section 6501 TRs exploited the addition of the gross receipts provision and ruled that "an understated amount of gross income resulting from an overstatement of unrecovered cost or other basis constitutes an omission from gross income [*when applied to trades or businesses*]."[112]

In 2012, in *Home Concrete*, the Supreme Court evaluated the final Section 6501 TRs, applying *Chevron* deference.[113] The Court concluded that its ruling in *Colony* was unambiguous and that the final Section 6501 TRs were therefore invalid.[114] However, the Court was left to address another unresolved issue that it first attempted to answer in *Brand X*: when is a court bound by prior determination of statutory ambiguity.[115] Although the *Home Concrete* decision ended the debate over *Colony*'s statutory interpretation of "omits from gross income," the Court's *Brand X* analysis was limited to a nonbinding plurality opinion.[116]

III. ANALYSIS

As detailed in Part II, the circuit split over extending the SOL under Section 6501 involved (1) the standard of deference applied to TRs, (2) whether *Colony* controlled the outcome of the Section's ambiguity, and (3) the validity of the Section 6501 TRs.[117] Accordingly, this Section will argue that the circuit split and the recent Supreme Court

111. Treas. Reg. §§ 301.6501(e)-1, 301.6229(c)(2)-1 (as amended T.D. 9511, 75 Fed. Reg. 78897-01 (Dec. 17, 2010)). Both the temporary TRs and the final TRs were largely a result of IRS litigation in *Bakersfield Energy Partners v. Commissioner*, 568 F.3d 767 (9th Cir. 2009). *See* Treas. Reg. §§ 301.6501(e)-1, 301.6229(c)(2)-1 (as amended T.D. 9511, 75 Fed. Reg. 78897-01 (Dec. 17, 2010)). In *Bakersfield Energy*, the Court refused to extend the SOL to six years, applying the *Colony* interpretation and limiting the extension to trades or businesses. However, the court noted that the Treasury "may have the authority to promulgate a reasonable interpretation of an ambiguous provision of the tax code, even if its interpretation runs contrary to the Supreme Court's opinion as to the best reading of the provision." *Bakersfield Energy*, 568 F.3d at 778.

112. Treas. Reg. §§ 301.6501(e)-1, 301.6229(c)(2)-1 (as amended T.D. 9511, 75 Fed. Reg. 78897-01 (Dec. 17, 2010)) (emphasis added). The final regulations were issued on December 17, 2010, and explicitly disagreed with the tax court's decision in *Intermountain Insurance Service of Vail v. Commissioner*, 134 T.C. 211 (2010), in which the tax court declared the temporary regulations invalid. *See id.*

113. *See* United States v. Home Concrete & Supply, LLC, 132 S. Ct. 1836, 1847 (2011); *Mayo Foundation*, 131 S. Ct. at 713 ("[T]he principles underlying our decision in *Chevron* apply with full force in the tax context.").

114. *See Home Concrete*, 132 S. Ct. at 1844.

115. *See* Grapevine Imports, Ltd. v. United States, 636 F.3d 1368, 1377-78 (2011) (discussing the impact of *Brand X* on the court's *Colony* analysis).

116. *See* United States v. Home Concrete & Supply, LLC, 132 S. Ct. 1836, 1842-43 (2011).

117. *See* Carpenter Family Invs., LLC v. Comm'r, 136 T.C. 373, 381 (2011) (implicitly arguing that, for a court to uphold the TRs, the court must create an ambiguity for the Treasury to regulate by applying the "trade or business" exception).

plurality decision demonstrate the failure of the *Brand X* framework and will present a methodology that can be used to avoid the *Brand X* problem in the future.

Section A of this Part will argue that *Brand X* is an important, yet ambiguous precedent. Part B will argue that *Brand X*'s ambiguity was implicated in all five Section 6501 cases decided by the circuit courts since the promulgation of the Section 6501 TRs. Part C will argue that none of the frameworks suggested in the literature[118] or used by the courts will produce consistent application of *Brand X*.[119] In fact, Part C will show that *Brand X* cannot be clarified using any framework that attempts to determine when a prior determination of statutory ambiguity has been made.[120]

Instead, as Part D will argue, courts should distinguish prior determinations of statutory ambiguity where possible, avoiding *Brand X* altogether. Finally, Part E will argue that avoiding the *Brand X* question and deferring to agencies whenever possible is the only way to ensure consistency in lower courts and faithfulness to *Chevron*'s deferential standard.[121]

A. Brand X: *An Important Precedent with Ambiguous Meaning*

Brand X attempted to resolve the tension between two countervailing judicial principles: *Chevron*'s deference to administrative agencies to interpret statutes on the one hand, and the judiciary's power "to say what the law is" on the other.[122] In *Brand X*, the Supreme Court held that a "court's prior judicial construction of a statute trumps an agency construction otherwise entitled to *Chevron* deference only if the prior court decision holds that its construction *follows from the unambiguous terms of the statute* and thus leaves no room for agency

118. *See Implementing Brand X: What Counts as a Step One Holding?*, 119 HARV. L. REV. 1532, 1539-40 (2006).

119. *Compare* Home Concrete & Supply v. United States, 634 F.3d 249, 257 (applying *Brand X* to conclude that *Colony* foreclosed agency regulation), *aff'd*, 132 S. Ct 1836 (2011), *with* Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929, 939 (applying *Brand X* to conclude that *Colony* did not foreclose agency regulation).

120. *See Carpenter Family Invs.*, 136 T.C. at 390 n.21 (discussing the chaotic nature of decisions since *Brand X*).

121. *See* Thomas W. Merrill & Kristin E. Hickman, *Chevron's Domain*, 89 GEO. L.J. 833, 918-19; Craig, *supra* note 31, at 18.

122. Marbury v. Madison, 5 U.S. 137, 177 (1803); *see* Nat'l Cable & Telecomms. Ass'n. v. Brand X Internet Servs., 545 U.S. 967, 1017 (2005) (Scalia, J., dissenting) ("Article III courts do not sit to render decisions that can be reversed or ignored by executive officers."); *see also* Brian G. Slocum, *The Importance of Being Ambiguous: Substantive Canons, Stare Decisis, and the Central Role of Ambiguity Determinations in the Administrative State*, 69 MD. L. REV. 791, 797 (2010).

discretion."[123] Therefore, a court applying the *Brand X* test asks whether the decision in the prior case determining statutory ambiguity followed from the unambiguous terms of the statute.[124] The test is important because it is possible that an agency regulation can trump binding judicial precedents, even when they contradict.[125] That is, a court interpreting *Brand X* can characterize a prior determination of statutory ambiguity as either: (1) a *Chevron* step-one holding, in which a statute is unambiguous, therefore foreclosing alternative interpretations; or (2) a *Chevron* step-two holding, in which the statute is ambiguous and the prior determination of statutory ambiguity represented but one reasonable interpretation.[126]

Commentators attempting to clarify the *Brand X* test disagree as to how cases decided before *Brand X* fit into the *Chevron* framework.[127] Similarly, courts have been unable to find a consistent framework to determine when a previously adjudicated prior case has made a binding determination of statutory ambiguity.[128] As a result, courts arbitrarily label a prior statutory interpretation of ambiguity either as: (1) binding, thus foreclosing agency regulation because the prior case took *the only* reasonable interpretation; or, (2) as not binding, thus allowing regulation because the prior case took *only a* reasonable interpretation.[129] This inconsistent application of the *Brand X* test is arguably a result of courts being unable to determine when a prior decision "follows from the unambiguous terms of the statute."[130]

Brand X is powerful because it can re-characterize what might otherwise be binding precedent.[131] *Brand X* attempts to create a framework to save appellate courts from re-characterizing where the

123. Nat'l Cable & Telecomms. Ass'n. v. Brand X Internet Servs., 545 U.S. 967, 982 (2005) (emphasis added).

124. *See id.*

125. *See* Richard Murphy, *The Brand X Constitution*, 2007 B.Y.U. L. REV. 1247, 1251 (2007).

126. *Compare* Home Concrete & Supply v. United States, 634 F.3d 249, 258 (Wilkinson, J., concurring) ("I believe that Colony was decided under Chevron step one."), *aff'd*, 132 S. Ct 1836 (2011), *with* Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929, 937-39 (10th Cir. 2011) (concluding that *Colony* is not conclusive regarding *Chevron* step-one, but rather a reasonable interpretation applied to the trade and business context).

127. *See Implementing Brand X*, *supra* note 118, at 1533 (2006).

128. *See Administrative Law*, *supra* note 32, at 1067.

129. *See Implementing Brand X*, *supra* note 118, at 1539-40 (2006).

130. Nat'l Cable & Telecomms. Ass'n. v. Brand X Internet Servs., 545 U.S. 967, 982 (2005); *see also Implementing Brand X*, *supra* note 118, at 1539-40 (discussing three tests for determining the applicability of a prior judicial determination of ambiguity); Craig, *supra* note 31, at 18-24 (comparing courts that deferred to agency regulation over jurisdictional precedents to those courts that did not).

131. *See* Murphy, *supra* note 125, at 1316.

court's prior decisions fit into *Chevron* analysis on a case-by-case basis.[132] However, *Brand X* also leaves parties without direction by weakening reliance on *stare decisis*.[133] Indeed, since the promulgation of the final Section 6501 TRs, the circuit courts have interpreted the meaning of *Colony* inconsistently, exemplifying the unworkability of *Brand X*.[134]

B. The Ambiguity of Brand X *is Apparent in the* Colony *Circuit Split*

The circuit split over Section 6501 and whether courts are bound by *Colony* demonstrates that judges are unable to apply *Brand X* consistently.[135] The divergent outcomes emanate from the courts' application of *Colony* as either a *Chevron* step-one or step-two holding.[136] Two courts implicitly applied *Colony* as a *Chevron* step-one holding.[137] In *Home Concrete*, the Fourth Circuit began its *Chevron* analysis by asking whether the Section 6501 TRs interpreted an ambiguous statute.[138] The court decided that *Colony* declared Section 6501 to be unambiguous, thus constituted binding precedent that the TRs could not displace.[139] Similarly, in *Burks v. United States*,[140] the court decided that *Colony* stood for the proposition that Section 6501 was unambiguous, rendering the TRs invalid.[141] Neither court found that the

132. *See Administrative Law*, *supra* note 32, at 1071-72 (explaining that *Brand X* would be problematic if applied inconsistently); Merrill & Hickman, *supra* note 121, at 919.

133. *Id.*

134. *See, e.g.*, Home Concrete & Supply, LLC v. United States, 634 F.3d 249, 255 (4th Cir. 2011) (discussing the ability of the Treasury to regulate in the wake of *Colony*), *aff'd*, 132 S. Ct 1836 (2011); *Administrative Law*, *supra* note 32, at 1072 (characterizing the majority and the dissent in Intermountain Insurance Service of Vail v. Commissioner, 650 F.3d 691, 707 (D.C. Cir. 2011), as "bickering" over the proper application of *Brand X*).

135. *Compare Home Concrete*, 634 F.3d at 254 (implicitly applying the "magic words" test, a Chevron step-one test to conclude that *Colony* was binding), *with* Grapevine Imports, Ltd. v. United States, 636 F.3d 1368, 1377-78 (Fed. Cir. 2011) (implicitly applying the "totality of the opinion" test to conclude that *Colony* was not binding).

136. *Compare Home Concrete*, 634 F.3d at 257 (applying *Colony* as a *Chevron* step-one holding, that the statute was unambiguous and for closing alternative interpretations), *with Grapevine Imports*, 636 F.3d at 1380 (applying *Colony* as a *Chevron* step-two holding, that the *Colony* provided a reasonable interpretation of the statute that would permit other regulatory interpretations).

137. *See Home Concrete*, 634 F.3d at 257; Burks v. United States, 633 F.3d 347, 360 (5th Cir. 2011).

138. *See Home Concrete*, 634 F.3d at 257.

139. *See id.* (applying *Brand X* implicitly by citation).

140. Burks v. United States, 633 F.3d 347 (5th Cir. 2011).

141. *See id.* at 360 (applying *Colony* without citing *Brand X*).

addition of the gross receipts provision in the 1954 I.R.C. limited the binding precedent of *Colony* to trades or businesses.[142]

Conversely, three circuits held that the TRs were valid by implicitly applying *Colony* as a *Chevron* step-two holding.[143] These courts found that *Colony* represented one reasonable interpretation of the statute, rather than the only reasonable interpretation of the statute.[144] In *Grapevine Imports, Ltd. v. United States*,[145] *Salman Ranch IV*, and *Intermountain Insurance Service of Vail v. Commissioner*,[146] the courts conducted a step-one *Chevron* analysis by examining the statutory language and legislative history.[147] The courts applied the *Brand X* test to determine whether *Colony* made a binding determination of statutory ambiguity. The courts emphasized the *Colony* Court's use of "ambiguous" and argued that *Colony* never purported to hold that its interpretation was the only interpretation that could follow from the statute.[148]

Notably, the three courts characterized *Colony*'s holding as limited by the gross receipts provision added in the 1954 I.R.C.[149] They argued that this provision's addition signaled Congress's intent to apply *Colony*'s exclusion of basis overstatement in "omits from gross income," reasoning that it applies only to trades or businesses.[150] Accordingly, in these three cases, the courts found that the gross receipts provision was inapplicable because they involved Son-of-BOSS transactions in

142. *See Home Concrete*, 634 F.3d at 254-55; *Burks*, 633 F.3d at 355-59.

143. *See* Grapevine Imports, Ltd. v. United States, 636 F.3d 1368, 1380 (Fed. Cir. 2011); Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929, 940 (10th Cir. 2011); Intermountain Ins. Serv. of Vail v. Comm'r, 650 F.3d 691, 707 (D.C. Cir. 2011).

144. *See, e.g.*, *Grapevine Imports*, 636 F.3d at 1380 ("*Colony*'s holding does not foreclose reasonable disagreement in agency rules under *Chevron*. Neither that case nor *Salman Ranch* found Congress's intent was so clear as to support no reasonable interpretation other than the taxpayer's.").

145. Grapevine Imports, Ltd. v. United States, 636 F.3d 1368 (Fed. Cir. 2011).

146. Intermountain Ins. Serv. of Vail v. Comm'r, 650 F.3d 691 (D.C. Cir. 2011).

147. *See Grapevine Imports*, 636 F.3d at 1376-80 ("[*Colony*,] while instructive, do[es] not resolve the question for purposes of Chevron step one."); *Salman Ranch IV*, 647 F.3d at 937-39; *Intermountain Ins.*, 650 F.3d at 701-07.

148. *See Grapevine Imports*, 636 F.3d at 1378-79; *Salman Ranch IV*, 647 F.3d at 937-39; *Intermountain Ins.*, 650 F.3d at 705-06. While *Chevron* step-one analysis asks whether a statute is ambiguous, congressional intent and legislative history are also considered in addition to statutory construction. *See* Anderson v. Dep't of Labor, 422 F.3d 1155, 1180 (10th Cir. 2005) (citing Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 843 n.9 (1984)).

149. *See* I.R.C. § 6501(e)(1)(A)(i) (2006); *Grapevine Imports*, 636 F.3d at 1378; *Salman Ranch IV*, 647 F.3d at 938; *Intermountain Ins.*, 650 F.3d at 705-06.

150. *See, e.g.*, *Intermountain Ins.*, 650 F.3d at 702-03 (concluding that Congress added I.R.C. § 6501(e)(1)(A)(i), the gross receipts provision, in the 1954 code so that overstatements of basis would not be included in "omits from gross income" in the trade or business context and, thus, *Colony* was not binding outside the trade or business context).

partnerships that were not trades or businesses within the meaning of the statute.[151]

The three circuit courts then conducted a *Chevron* step-two inquiry, asking whether the agency's interpretation was reasonable.[152] The courts determined that, outside the trade or business context, it is reasonable to assume that Congress would have included an overstatement of basis as "omits from gross income" because gross income is determined by subtracting the basis from the amount realized on an item sold.[153] The courts explicitly declined to adopt *Colony*'s interpretation outside the trade or business context.[154]

The inability of the courts to determine whether *Colony* had made a binding determination of Section 6501's ambiguity caused the circuit split.[155] The courts focused on where the prior decision fit into the *Chevron* analysis.[156] *Brand X*'s attempt to determine when a court was bound by a pre-existing determination of statutory ambiguity failed.[157] However, the circuit courts might have produced consistent interpretations of *Colony* if a workable framework existed that could consistently apply the *Brand X* test.

C. *No Formulation of the* Brand X *Test Will Yield Consistent Results*

Under *Brand X*, a prior determination of statutory ambiguity should only bind a court if the earlier court found that the statute was unambiguous: a *Chevron* step-one holding.[158] As discussed, courts have

151. *See Grapevine Imports*, 636 F.3d at 1372; *Salman Ranch IV*, 647 F.3d at 932-33; *Intermountain Ins.*, 650 F.3d at 695.

152. *See Grapevine Imports*, 636 F.3d at 1380; *Salman Ranch IV*, 647 F.3d at 939; *Intermountain Ins.*, 650 F.3d at 707.

153. *See* I.R.C. § 1001 (2006); *Grapevine Imports*, 636 F.3d at 1380; *Salman Ranch IV*, 647 F.3d at 940; *Intermountain Ins.*, 650 F.3d at 707. The courts also examined legislative intent and reasoned that the addition of the gross receipts provision in 1954 rendered Section 6501 meaningless without limiting *Colony* to the trade or business context. *See, e.g.*, *Grapevine Imports*, 636 F.3d at 1380 (discussing legislative intent).

154. *See Grapevine Imports*, 636 F.3d at 1380; *Salman Ranch IV*, 647 F.3d at 940; *Intermountain Ins.*, 650 F.3d at 707.

155. *See* Burks v. United States, 633 F.3d 347, 360 (5th Cir. 2011); Home Concrete & Supply, LLC v. United States, 634 F.3d 249, 257 (4th Cir. 2011), *aff'd*, 132 S. Ct 1836 (2011); *Grapevine Imports*, 636 F.3d at 1380; *Salman Ranch IV*, 647 F.3d at 940; *Intermountain Ins.*, 650 F.3d at 707.

156. *See Burks*, 633 F.3d at 360; *Home Concrete*, 634 F.3d at 257; *Grapevine Imports*, 636 F.3d at 1380; *Salman Ranch IV*, 647 F.3d at 940; *Intermountain Ins.*, 650 F.3d at 707.

157. *See Burks*, 633 F.3d at 360; *Home Concrete*, 634 F.3d at 257; *Grapevine Imports*, 636 F.3d at 1380; *Salman Ranch IV*, 647 F.3d at 940; *Intermountain Ins.*, 650 F.3d at 707.

158. *See* Nat'l Cable & Telecomms. Ass'n. v. Brand X Internet Servs., 545 U.S. 967, 982 (2005) ("A court's prior judicial construction of a statute trumps an agency construction otherwise entitled to Chevron deference only if the prior court decision

taken divergent approaches when deciding what constitutes a prior *Chevron* step-one holding, and courts have applied none of them consistently.[159]

Commentators have suggested several frameworks in which courts could apply *Brand X* with consistency.[160] However, applying these frameworks to Section 6501 reveals that it is impossible to create consistency by deciding when a prior construction of statutory ambiguity constitutes a *Chevron* step-one holding.[161]

First, courts could look for "magic words" in an opinion, finding a binding determination of a statute's ambiguity—a *Chevron* step-one holding—any time the case refers to statutory language as "clear" or "unambiguous."[162] The Section 6501 cases demonstrate the futility of the magic words approach.[163] For example, in *Home Concrete*, the Fourth Circuit interpreted *Colony*'s use of the word "unambiguous" as referring to all applications of Section 6501.[164] Similarly, the Court in *Salman Ranch IV* referred to *Colony*'s use of "unambiguous."[165] However, that Court came to an entirely different conclusion: *Colony* holds that the only ambiguous part of Section 6501 was the provision referring to an overstatement of basis in the trade or business context.[166] The *Salman Ranch IV* Court, therefore, focused on *Colony*'s use of "ambiguous" as it referred to the statute outside the trade or business context.[167]

Second, courts could use a "totality of the opinion" approach, asking whether the pre-*Chevron* court would have held that the statute

---

holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion.").

159. *See* Home Concrete & Supply, LLC v. United States, 634 F.3d 249, 260 (Wilkinson, J., concurring) (acknowledging the disruption that the circuit split has caused in the *Chevron*, *Brand X*, and *Mayo Foundation* continuum).

160. *Contra Administrative Law*, *supra* note 32, at 1073 (arguing that the "if necessary" test would result in equal application of *Brand X*).

161. *See* Burks v. United States, 633 F.3d 347, 353-54 (5th Cir. 2011) (citing the divergent opinions in Section 6501 cases).

162. *See Implementing Brand X*, *supra* note 118, at 1539-40.

163. *See, e.g.*, *Home Concrete*, 634 F.3d at 259 (Wilkinson, J., concurring) (concluding that *Colony*'s use of "unambiguous" could not be ignored, even though the court also defined the statute as "ambiguous").

164. *See id.* at 257 (majority opinion).

165. *See* Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929, 938 (10th Cir. 2011).

166. *See id.*

167. *See id*; *see also* United States v. Home Concrete & Supply, LLC, 132 S. Ct. 1836, 1847 (Scalia, J., concurring) (2011) ("In cases decided pre-*Brand X*, the Court had no inkling that it must utter the magic words 'ambiguous' or 'unambiguous' in order to (poof!) expand or abridge executive power, and (poof!) enable or disable administrative contradiction of the Supreme Court.").

was ambiguous if it were applying *Chevron* "counterfactually."[168] As with elements of the "magic words" approach, there are elements of the "totality of the opinion" approach in Section 6501 cases that demonstrate its futility as a possible *Brand X* framework.[169] The problems with this approach are evidenced in the Tax Court's most recent case, *Carpenter Family Investments v. Commissioner*,[170] in which the Court implicitly attempted to evaluate *Colony* as if it had decided post-*Chevron*.[171] Although the Tax Court eventually concluded that *Colony* determined Section 6501 was unambiguous, its analysis could not be applied consistently.[172] The court lingered on the appropriateness of *Colony*'s use of legislative history to divine congressional intent, the policy considerations behind *Colony*'s interpretation, and whether *Brand X* could displace a Supreme Court precedent.[173] Considering such diverse factors makes the totality of the opinion approach too convoluted to apply consistently.[174]

Finally, courts could find a binding determination of ambiguity—a *Chevron* step-one holding—when the previous court "could have only reached the result it did by holding that its interpretation was the only reasonable one."[175] That is, courts should find a binding *Chevron* step-one holding only when the previous court's interpretation of the statute's ambiguity was "necessary" to its holding.[176] However, it is difficult to imagine a situation in which a court would have to determine that a finding of no ambiguity was necessary for its holding; rather, the more likely conclusion will be that the court's reasonable interpretation was

168. *See* Merrill & Hickman, *supra* note 121, at 917; *Implementing Brand X*, *supra* note 118, at 1539.

169. *See Administrative Law*, *supra* note 32, at 1072.

170. Carpenter Family Invs., LLC. v. Comm'r, 136 T.C. 373 (2011).

171. *See id.* at 390-94.

172. *See id.* This conclusion was a step-one holding. *See id.*

173. *See id.* at 389-90, 394. In a concurring opinion to *Brand X*, Justice Stevens noted that lower courts might not be able to displace a statutory interpretation by the Supreme Court because of the precedential power of its decisions. *See* Nat'l Cable & Telecomms. Ass'n. v. Brand X Internet Servs., 545 U.S. 967, 1003 (2005) (Stevens, J., concurring) ("[*Brand X*'s reasoning] would not necessarily be applicable to a decision by this Court that would presumably remove any pre-existing ambiguity.").

174. *See Administrative Law*, *supra* note 32, at 1072.

175. *See Implementing Brand X*, *supra* note 118, at 1540-47 (emphasis added) (concluding that the "if necessary" test is best because it has low decision costs, a high degree of "accurate statutory interpretation," and it correctly balances stability of judicial precedent with the agency flexibility).

176. *See Administrative Law*, *supra* note 32, at 1072 (explaining that a case-by-case totality of the opinion approach "would likely lead to deep intercircuit disagreement").

necessary for its holding.[177] Therefore, it will be difficult to apply the "if necessary" test with consistency.

As discussed above, the varied approaches that commentators have advocated for *Brand X* consistency are untenable in light of the Section 6501 cases.[178] Courts should not inquire when pre-existing precedent applies, or where it constitutes a *Chevron* step-one or *Chevron* step-two conclusion. Instead, courts should avoid the question by limiting the prior court's construction as narrowly as possible.[179]

D. Courts Can Only Achieve Consistency by Distinguishing Precedent When Possible

The different results in the circuit courts emanate from different interpretations of the *Brand X* test for when a prior precedent determining statutory ambiguity should bind a subsequent court.[180] The circuit courts' decisions focus on determining if *Colony*'s "construction follows from the unambiguous terms of the statute."[181] This focus resulted in courts treating the trade and business exception differently, demonstrating that the current *Brand X* jurisprudence is impossible to consistently construe.[182]

Although the essence of the circuit split was the application of *Colony* as a *Chevron* step-one or step-two holding, each court's conclusion was grounded in its willingness to distinguish *Colony* based

177. *Contra id.* at 1073 n.65. In support of the "if necessary" test, the author cited a case "interpreting a prior court's analysis as a holding because it was not a 'stray mark or aside.'" *Id.* (citation omitted). However the author does not explain how the "if necessary" test would apply in any other practical scenario. *See id.* at 1066-73.

178. *See id.* at 1066 (criticizing a *Brand X* test that would ask "what the court would have held had it decided the case after *Chevron* was handed down").

179. *See infra* Part III.E.

180. *See* Nat'l Cable & Telecomms. Ass'n. v. Brand X Internet Servs., 545 U.S. 967, 982 (2005) ("A court's prior judicial construction of a statute trumps an agency construction otherwise entitled to Chevron deference only if the prior court decision holds that its construction follows from the unambiguous terms of the statute and thus leaves no room for agency discretion.").

181. *See, e.g.*, Grapevine Imports, Ltd. v. United States, 636 F.3d 1368, 1379 (Fed. Cir. 2011) (citing *Brand X* to determine where *Colony* fits into the *Chevron* analysis). Although not all the circuit courts explicitly used *Brand X*, all at least implicitly applied *Brand X* by asking whether *Colony* constituted a binding determination of statutory ambiguity. *See, e.g.*, Intermountain Ins. Serv. of Vail v. Comm'r, 650 F.3d 691, 703 (D.C. Cir. 2011) (discussing the effect of *Colony* on the *Chevron* analysis without actually citing *Brand X* in the opinion).

182. *Id. Compare* Home Concrete & Supply, LLC v. United States, 634 F.3d 249, 257, 257 (4th Cir. 2011) (applying *Brand X* to conclude that *Colony* foreclosed agency regulation), *aff'd*, 132 S. Ct 1836 (2011), *with* Salman Ranch IV, 647 F.3d at 939 (applying *Brand X* to conclude that *Colony* did not foreclose agency regulation).

on the trade or business exception.[183] The circuit courts that refused to extend the SOL characterized *Colony* as applying to any overstatement of basis, regardless of whether the entity was a trade or business.[184] By contrast, the courts that extended the SOL to six years found that *Colony* was only a reasonable interpretation of Section 6501, and that the Section 6501 TRs represented another reasonable interpretation.[185] Instead of resting their decision on the binding power of *Colony*, the courts should have considered, before moving to the *Chevron* and *Brand X* analysis, whether the court could distinguish *Colony*, thus avoiding an analysis that asks whether *Colony* made a determination of statutory ambiguity altogether. Applying this framework, the courts would only need to examine the binding power of *Colony* in the trade or business context, and would be able to distinguish *Colony* outside the trade or business context.[186]

In *Home Concrete*, the Supreme Court failed to apply *Brand X*.[187] Instead, the Court implicitly engaged in a *Brand X* analysis by asking if *Colony* made a binding determination of statutory ambiguity. The Court attempted to avoid determining whether *Colony* represented a *Chevron* step-one or step-two holding, and instead purported to rest its decision on *stare decisis*.[188] However, the Court did not successfully avoid *Chevron* or *Brand X*.[189] In fact, aside from distinguishing precedent, it is impossible to avoid *Brand X* because any implicit determination on the binding authority of a prior court's ambiguity determination will necessarily implicate *Brand X*.[190]

The Supreme Court held that Section 6501 was unambiguous in all contexts. The Court decided *Colony*'s meaning without explaining why the case constituted a binding determination of ambiguity.[191] The Court

183. *See* Burks v. United States, 633 F.3d 347, 360 (5th Cir. 2011); *Home Concrete*, 634 F.3d at 257; *Grapevine Imports*, 636 F.3d at 1380; *Salman Ranch IV*, 647 F.3d at 940; *Intermountain Ins.*, 650 F.3d at 707.

184. *See Burks*, 633 F.3d at 360; *Home Concrete*, 634 F.3d at 257.

185. *See Grapevine Imports*, 636 F.3d at 1380; *Salman Ranch IV*, 647 F.3d at 940; *Intermountain Ins.*, 650 F.3d at 707.

186. *See, e.g.*, *Salman Ranch IV*, 647 F.3d at 939 ("While we know now what "omits from gross income" means in § 6501(e)(1)(A) when a trade or business is involved because of subparagraph (i), it is still far from clear what Congress intended it to mean in other contexts.").

187. *Accord* Richard Lipton & Russell Young, *Supreme Court's Decision in Home Concrete Reveals Cracks in the Foundation of Brand X*, 117 J. TAX'N 4, 4 (2012) ("As a result of the divided court in Home Concrete, the application of Brand X in future cases is highly uncertain.").

188. *See* United States v. Home Concrete & Supply, LLC, 132 S. Ct. 1836, 1841 (2011) (purporting that the decision of the case rests on *stare decisis*).

189. *See Home Concrete*, 132 S. Ct. at 1847 (Scalia, J., concurring).

190. *See id.* at 1848.

191. *See Home Concrete*, 132 S. Ct. at 1841.

implicitly applied *Brand X* by holding that that the Supreme Court's prior interpretation of Section 6501 was a binding determination of statutory ambiguity.[192] However, the Court did not explain why *Colony* constituted a *Chevron* step-one holding—that Section 6501 was unambiguous—which may lead to continuing frustration.[193]

If the Supreme Court did not want to engage in a *Brand X* analysis, the Court could have avoided the *Brand X* question entirely by limiting *Colony* to trades or businesses.[194] If the Supreme Court had limited *Colony* to trades or businesses, the Court would have resolved the case before reaching *Chevron* and *Brand X*, and avoided whether *Colony* constituted a binding decision of statutory ambiguity.[195] By distinguishing precedent, the court could have avoided the *Brand X* confusion entirely.

Distinguishing prior precedent is necessary because, as the Section 6501 cases demonstrate, frameworks that have attempted to clarify when a court's interpretation "followed from the unambiguous terms of the statute" have failed.[196] Instead, by construing ambiguity precedents narrowly, courts will be consistent with *Chevron* deference jurisprudence and will limit the frequency in which courts confront the impossible *Brand X* question.[197]

E. *Avoiding* Brand X *Will Ensure Consistency in Lower Courts and Faithfulness to* Chevron

In *Home Concrete*, the Supreme Court could have held that *Colony*'s mandate was limited to taxpayers that are trades or businesses before attempting to decide whether the case constituted a binding

192. *See id.* at 1843. The Court lays out the Treasury's argument, explaining the Court's decision in one statement: "In our view, *Colony* has already interpreted the statute, and there is no longer any different construction that is consistent with *Colony* and available for adoption by the agency." *Id.* at 1841.

193. *See* Brief for Respondents, United States v. Home Concrete & Supply, 132 S. Ct. 1836 (2012) (No. 11-139), 2011 WL 6325858, at *i; *Home Concrete*, 634 F.3d at 258 (Wilkinson, J., concurring) (acknowledging that "it is sometimes difficult to determine whether pre-*Chevron* decisions are based upon '*Chevron* step one'"); Lipton & Young, *supra* note 187, at 4.

194. *See* Lipton & Young, *supra* note 187, at 10 ("While the court cited *Brand X* . . . nothing in the majority opinion indicates why *Colony* does not present a situation where a judicial interpretation must give way to a conflicting agency interpretation.").

195. *See* Lipton & Young, *supra* note 187, at 9 (asking whether the Supreme Court's reliance on *Colony* in *Home Concrete* "in the face of Regulations" is consistent with *Brand X* because "Colony was actually interpreting an unambiguous statute[]"); *Brand X*, 545 U.S. at 982.

196. *See supra* Part III.C.

197. *See generally Home Concrete*, 634 F.3d at 254-55 (discussing the relationship between the trade and business exception and *Colony*).

determination of statutory ambiguity under *Brand X*.[198] The Court would have thus avoided the internal disagreement over the *Brand X* question, which is evidenced by *Home Concrete*'s plurality, concurrence, and dissent.[199] If the Supreme Court confronts a similar question, it could distinguish the prior determination of statutory ambiguity before reaching the *Brand X* question. Such a holding will achieve two objectives. First, it will provide a standard that will result in circuit court decision constituency when applying *Brand X*.[200] Second, the holding will ensure that the spirit of *Chevron* is followed by granting administrative agencies, including the Treasury, deference in their area of expertise.[201]

Limiting the extent of judicial precedent in a *Brand X* inquiry will produce consistent results.[202] Conversely, any test that requires a court to reclassify holdings from prior cases would be "fraught with difficulties."[203] Courts would be able to avoid the question of precedential value of the prior judicial determination of statutory ambiguity if they limit the application of a decision in its entirety.[204]

The second advantage of clarifying that a court is only narrowly bound to a prior determination of statutory ambiguity is that the standard will continue the *Chevron* spirit of administrative deference.[205] In *Chevron*, the Supreme Court reasoned: similar to how Congress is better suited than the courts in making policy, administrative agencies are better suited than the courts at interpreting statutes in accordance with policy.[206] *Brand X* reaffirmed *Chevron* and created a deferential approach to resolving judicial conflicts of an agency's statutory interpretation.[207] Subsequently, *Mayo Foundation* brought TR deference within the *Chevron* framework, eliminating the less deferential *National Muffler* standard.[208] In the wake of the Supreme Court's

198. *See* Brief for United States, United States v. Home Concrete & Supply, 132 S. Ct. 1836 (2012) (No. 11-139), 2011 WL 5591822, at *46 ("In enacting subparagraph (i), by contrast, Congress established a special definition of gross income that applies only in the case of a trade or business.") (internal quotation marks and citations omitted).

199. *See* United States v. Home Concrete & Supply, LLC, 132 S. Ct 1836, 1843-52 (2011).

200. *See* Merrill & Hickman, *supra* note 121, at 18.

201. *See* Craig, *supra* note 31, at 18.

202. *See Administrative Law*, *supra* note 32, at 1072 ("The problem of reexamination, of course, would exist under any regime that mandated recategorization of past statutory interpretation.").

203. *See* Merrill & Hickman, *supra* note 121, at 918-19.

204. *See id.*

205. *See* Craig, *supra* note 31, at 18.

206. *See* Murphy, *supra* note 125, at 865-66.

207. *See Administrative Law*, *supra* note 32, at 1070 (2011).

208. Mayo Found. for Med. Educ. & Research v. United States, 131 S. Ct. 704, 713 (2011).

acknowledgement in *Mayo Foundation* that the Treasury deserves a high level deference to its regulations, the circuit courts have disagreed on how far that deference should go.[209] The Supreme Court's jurisprudence has continually reaffirmed administration deference.[210] By holding that a pre-*Chevron* determination of statutory ambiguity should be limited as narrowly as possible, the Supreme Court will adhere to its continuing deferential jurisprudence.[211]

Although limiting precedent is preferable, it is admittedly problematic. On one hand, *Colony* is binding within the trade or business context because *Colony* declared Section 6501 to be unambiguous.[212] On the other hand, *Colony* is not binding outside the trade or business context because Section 6501 is ambiguous.[213] This divergence is an intellectual conundrum because courts will be holding the statute ambiguous in one context and unambiguous in another.[214] However, by limiting the precedential nature of a prior determination of statutory ambiguity, rather than delving into *Brand X*, courts will produce consistent results and will be faithful to *Chevron* deference.[215]

IV. CONCLUSION

Regulation by administrative agencies is an essential part of interpreting vague statutes.[216] If there is ambiguity in a law, Congress permits agencies to resolve the ambiguity.[217] Agency interpretation, however, is checked when courts use the *Chevron* framework to determine the scope and reasonableness of regulation.[218]

---

209. *Compare* Home Concrete & Supply, LLC v. United States, 634 F.3d 249 (4th Cir. 2011) (acknowledging *Mayo Foundation*, but declining to defer to the Section 6501 TRs), *aff'd*, 132 S. Ct 1836 (2011), *with* Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929 (10th Cir. 2011) (deferring to the Section 6501 TRs).

210. *See, e.g.*, *Mayo Found.*, 131 S. Ct. at 713 (reaffirming *Chevron* by extending the doctrine to TR deference).

211. *See* Craig, *supra* note 31, at 18.

212. *See* Colony, Inc. v. Comm'r, 357 U.S. 28, 37 (1958).

213. *See, e.g.*, *Salman Ranch IV*, 647 F.3d at 938 ("While the Partnership is correct that the Court later referred to the updated § 6501(e)(1)(A) (1954) as 'unambiguous,' . . . we do not read that analysis as extending beyond the trade-or-business context.").

214. *See* Carpenter Family Invs., LLC. v. Comm'r, 136 T.C. 373, 381 (2011) ("If the *Colony* holding has been statutorily confined to a trade or business context, it cannot any longer constitute the Supreme Court's interpretation of current Section 6501. Conversely, if *Colony* represents the Supreme Court's own construction of this text, the holding must necessarily extend beyond just trade or business.").

215. *See* Merrill & Hickman, *supra* note 121, at 918-19.

216. See Roche, *supra* note 3, at 263.

217. *See, e.g.*, I.R.C. § 7805(a) (2006) (granting the Treasury general interpretive authority over the I.R.C.).

218. *See* Chevron, U.S.A., Inc. v. Natural Res. Def. Council, Inc., 467 U.S. 837, 842-43 (1984).

Congress bestowed vast regulatory authority to the Treasury to interpret the I.R.C.[219] Although the power is legitimately used to prevent the abuse of tax shelters, Congress has limited the Treasury's power by imposing SOLs on the time the agency has to recoup deficiencies.[220] But when judicial precedent and agency interpretation conflict over the meaning of a statute, the taxpayer must take the risk that his action might go unnoticed, or incur expenses defending his return to sort out the conflict between the judiciary and the agency.[221]

The *Brand X* test attempts to determine when a pre-existing judicial determination of statutory ambiguity binds a court, rather than allowing deference to agency regulation.[222] However, the circuit split over Section 6501 demonstrated the fallibility of *Brand X*.[223] Two circuits decided to follow *Colony* in all contexts, holding that they were bound by *Colony*'s determination that Section 6501 was ambiguous.[224] Conversely, three circuits decided that they were not bound by *Colony* because the case represented one of many reasonable interpretations of the statute.[225] Although the Supreme Court attempted to avoid the *Brand X* question by purportedly basing its decision on *stare decisis*, the Court allowed the *Brand X* confusion to continue by implicitly deciding that *Colony* was unambiguous and controlling.[226]

If the Supreme Court reconsiders the issue of whether a prior determination of statutory ambiguity is binding, the Court should rule to limit the effect of precedent.[227] Limiting a pre-existing determination of statutory ambiguity to the narrowest grounds possible and distinguishing

---

219. *See* I.R.C. § 7805(a) (2006).

220. *See* Roche, *supra* note 3, at 263; I.R.C. § 6501(e)(1)(A) (2006).

221. *See* Transcript of Oral Argument at 22-23, United States v. Home Concrete & Supply, 132 S. Ct. 1836 (2012) (No. 11-139) (Breyer, J.: "Then look at the unfairness of [the Section 6501 TRs] . . . people spent a lot of money [defending their payment]. . . . And then . . . after continuous litigation, the IRS promulgates a regulation which tries to reach back and capture people who filed their return 9 years before.").

222. *See* Nat'l Cable & Telecomms. Ass'n. v. Brand X Internet Servs., 545 U.S. 967, 982 (2005).

223. *See Administrative Law*, *supra* note 32, at 1066-67 (using the Section 6501 circuit split to argue for a new *Brand X* framework).

224. *See* Burks v. United States, 633 F.3d 347, 360 (5th Cir. 2011); Home Concrete & Supply, LLC v. United States, 634 F.3d 249, 257 (4th Cir. 2011), *aff'd*, 132 S. Ct 1836 (2011).

225. *See* Grapevine Imports, Ltd. v. United States, 636 F.3d 1368, 1380 (Fed. Cir. 2011); Salman Ranch, Ltd. v. Comm'r (Salman Ranch IV), 647 F.3d 929, 940 (10th Cir. 2011); Intermountain Ins. Servs. of Vail v. Comm'r, 650 F.3d 691, 707 (D.C. Cir. 2011).

226. United States v. Home Concrete & Supply, LLC, 132 S. Ct. 1836, 1843 (2011).

227. In the alternative, the Court could overturn *Brand X* and eliminate this unnecessary wrinkle in *Chevron* jurisprudence, as advocated by Scalia's concurring opinion in *Home Concrete*. *See Home Concrete*, 132 S. Ct. at 1848 (Scalia, J., concurring).

in favor of agency regulation will avoid *Brand X*, yielding consistent results in lower courts that remain faithful to *Chevron* deference.[228]

This analysis of the Section 6501 split has provided an answer to the *Brand X* problem: when subsequent cases cannot be distinguished, *stare decisis* should rule the day; but, when subsequent cases can be distinguished, a court should limit pre-existing determinations of statutory ambiguity narrowly and allow agencies to regulate.

228. *See* Merrill & Hickman, *supra* note 121, at 918-19; Craig, *supra* note 31, at 18.

***